



**FINAL CROATIA PROGRAM REPORT  
TO  
U.S. AGENCY FOR INTERNATIONAL  
DEVELOPMENT**



**Cooperative Agreement NIS-A-00-97-00026-00  
June 1, 1997 – April 30, 2001  
\$7,200,816**

***Strengthened Private Enterprises in War-Affected  
Areas of Croatia  
(The FLAG Croatia Program)***

**July 2001**

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## **A. INTRODUCTION**

This is the final program report for activities in Croatia under USAID Cooperative Agreement NIS-A-97-00026-00 – “*Strengthened Private Enterprises in War-Affected Areas of Croatia*” (hereafter referred to as the “Program”). The initial award was signed between USAID and the University of Delaware (UD) on May 31, 1997. The report provides a review of activities and results over the 47 months of the Program, and was prepared by FLAG International, LLC (FI). Since January 1, 2001, FI has performed all services to fulfill obligations within the Program scope of work under a Cooperator Agreement with the University of Delaware.

As with many multi-year projects, our scope of work was periodically amended to reflect changing conditions and opportunities, new strategic frameworks within the USAID/Zagreb Mission, and improved approaches to strengthening small and medium-sized enterprises (SMEs) based on best practices and lessons learned. As a result, the Program was implemented in three distinct phases that reflected the movement of refugees and displaced persons (DPs) within the former United Nations Protected Areas (UNPAs), and the revised strategic frameworks and priorities within USAID. The three phases are:

- Phase 1 (June 1997 to November 1998), focused on reintegrating populations and enterprises in former UNPAs East and West;
- Phase 2 (December 1998 to December 1999), focused on reintegrating populations and strengthening enterprises in the four primary war-affected areas in Croatia (former UNPAs North, South, East and West);
- Phase 3 (January 2000 to April 30, 2001), focused on reintegration of populations and economic development projects in targeted municipalities within the four primary war-affected areas.

The following report describes Program activities in each of the three phases, including technical assistance strategies and results achieved. A summary is also provided to document lessons learned and recommendations for continued activities.

In addition to UD, the prime award recipient, five partner organizations recruited volunteer executives and advisors to provide technical assistance: International Executive Service Corps (IESC), Agricultural Cooperative Development International/Volunteers in Overseas Cooperative Assistance (ACDI/VOCA), MBA Enterprise Corps (MBAEC), Citizens Democracy Corps (CDC), and Land O’Lakes, Inc. (LoL).

## **Summary Program Activities and Results (June 1997 – April 2001)**

- 17% Annual Increase in Employment for 210 SME Clients (1,320 Jobs Created)
- 11% Annual Increase in Sales for 210 SME Clients
- 11 Farmers' Organizations transformed into Modern Agricultural Cooperatives
- 42 Farmers' Organizations Registered
- 880 Business (Trade) Linkages Established
- 75 Seminars with 2,790 Participants
- 91 US Volunteer Assignments
- 123 Local Consultant Assignments
- 12 Economic Development Grant Projects Completed
- 6 Municipal Economic Surveys Completed
- 3,700 Program Beneficiaries (including client firms, seminar participants, and members of farmers' organizations and agricultural cooperatives).

## **B. PROJECT BACKGROUND**

The original Cooperative Agreement was signed between USAID and the University of Delaware (UD) on May 31, 1997. The original Agreement was modified 11 times. Activities in Croatia were extended to March 31, 2001, with approval of modification 10 on December 14, 2000. The USAID/W Contract Specialist and Mission Director approved a final one-month, no-cost extension for activities in Croatia on March 20, 2001.

### **Modification 01**

The purpose of modification 01, in September 1997, was to incrementally fund the Agreement to fully fund the Program.

### **Modification 02**

The purpose of modification 02, in April 1998, was to replace the original program description in its entirety with a revised program description. This was a no-cost revision to the Program. The revised program description was necessary because of a revised USAID/Zagreb strategic framework. Four second-tier intermediate results and corresponding indicators and targets were included in the modification.

### **Modification 03**

The purpose of modification 03, in December 1998, was to increase the total estimated cost of the Agreement, to revise the program description and incorporate a revised budget, to extend the Agreement date to December 31, 1999, and to add incremental funding to fully fund the Program. Major revisions included extending the program to former UNPAs North and South, modifying the staffing plan, a change in the title of the program, and a revision of the impact indicators and related targets.

### **Modification 04**

The purpose of modification 04, in June 1999, was to incorporate a supplemental program description and revised budget to reflect program activities in Montenegro. This was a no-cost extension.

#### Modification 05

The purpose of this modification, in September 1999, was to provide a no-cost extension to the Montenegro activities included in the agreement by modification 04.

#### Modification 06

The purpose of modification 06, in December 1999, was to incorporate additional program descriptions and to increase the estimated cost of the Agreement. The Agreement was also extended to December 31, 2000. The program description and budget incorporated a local economic development grant (EDP) component to capitalize farmers' organizations and agricultural cooperatives.

#### Modification 07

The purpose of this no-cost modification in February 2000 was to modify the existing source/origin/nationality code on procurements by including geographical code 935 (Free World). The modification also approved procurement of agricultural commodities and equipment for local economic development grant projects.

#### Modification 08

The purpose of modification 08, in June 2000, was to provide incremental funding for activities in Montenegro.

#### Modification 09

The purpose of modification 09, in August 2000, was to provide incremental funding for activities in Montenegro.

#### Modification 10

The purpose of modification 10, in December 2000, was to increase the total estimated Program amount, revise program descriptions, incorporate a revised budget, and extend the Agreement completion date to December 31, 2001. The modification also added incremental funding. Major revisions included establishing a three-month closeout plan for program activities in Croatia, and an extension of the Montenegro program to December 31, 2001.

#### Modification 11

The purpose of modification 11, in May 2001, was to add incremental funding for program activities in Montenegro.

## **C. PHASE 1 ACTIVITIES AND RESULTS (June 1997 to November 1998)**

### **C.1 Strategy and Program Implementation (Phase 1)**

At the time of project design and award, the United Nations administered Eastern Slavonia, Baranja, and Western Sirmium.<sup>1</sup> The Program was part of the US strategy to support the return of displaced persons and refugees to the war-affected areas of Croatia. The goal of our Program was to strengthen private enterprises within the UN-administered areas and to facilitate their economic reintegration into Croatia. The Program was designed to begin two weeks prior to the end of the UN mandate on June 15, 1997. The UN mandate was eventually extended by seven months and ended on January 15, 1998.

Phase 1 Program strategy and goals concentrated on providing technical assistance to strengthen SMEs to facilitate the reintegration of the war-affected areas in former UNPAs East and West. The majority of the companies in these war-affected areas were small, with fewer than 25 employees. Our implementation plan included numerous reintegration outreach projects and seminars targeting small and medium-sized enterprise (SME) clients and farmers' organizations. Training and technical assistance projects and assignments were individually designed and implemented by local professional staff and resident expatriate advisors to assist privately owned SMEs and independent farmers' organizations. The Program was headquartered in Osijek, Croatia with regional Business Advisory Centers located in Vukovar and Daruvar.

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<sup>1</sup> The United Nations Transitional Authority in Eastern Slavonia, Baranja, and Western Sirmium (UNTAES) was established on January 15, 1996. UNTAES was established with military and civilian components to supervise and facilitate the demilitarization; monitor return of refugees; establish a temporary police force; undertake tasks related to civil administration and public services; organize elections; and undertake other activities relevant to the 1995 Basic Agreement (referred to as the "Erdut Agreement") providing for the peaceful reintegration of this region into Croatia.

**Chart No. 1: (Phase 1 Strategic Framework, Indicators and Targets) USAID/Croatia Strategic Objective (SO) 1:**  
Reintegration of Populations Affected by the Erdut Agreement

**Intermediate Result (I.R.) 1.1**

**Affected Populations Become Economically  
Productive Members of Society**

**I.R.1.1.1:**

Enterprise Growth  
and Expansion

**Indicator:** Number of  
assisted firms

**Target:** 30

**Indicator:** Sales growth  
in client firms

**Target:** 15%

**Indicator:** Employment  
growth in client firms

**Target:** 10%

**I.R.1.1.2:**

Reintegration of  
Regional Economies

**Indicator:** Number of  
linkages connecting firms  
in war-affected areas to  
other parts of Croatia

**Target:** 150

**I.R.1.1.3:**

Cooperatives and  
Farmers' Organizations  
Strengthened

**Indicator:** Number of new  
coops or associations  
developed

**Target:** 8

**Indicator:** Increase in sales  
for assisted agricultural  
cooperatives and associations

**Target:** 10%

**I.R.1.1.4:**

Policy and Regulatory Agendas  
Developed by Assisted Industry  
Associations

**Indicator:** Total number of members of  
assisted associations

**Target:** 3,000

**Indicator:** Policy and regulatory issues  
identified and solutions proposed and  
submitted

**Target:** 4

## C.2 Program Components (Phase 1)

To implement and accomplish the strategy and goals, our activities were organized into four core program components:

- Firm-Level Technical Assistance;
- Establishing Independent Farmers' Organizations and Modern Cooperatives;
- Outreach Training for Accountants;
- Business Linkage Activities.

### a. Firm-Level Technical Assistance:

Border crossing remained closed until January 15, 1998 and during this period Program activities focused technical assistance and training on company management and accountants in adjusting to the new tax regulations and accounting standards. We also focused technical assistance to prepare business plans and investment proposals to attract debt and equity financing for SMEs within the former UNPAs.

We selected 20 initial SME clients after completing a diagnostic evaluation on more than 90 companies in former UNPAs East and West. Once companies were selected and expressed interest in technical assistance, we assigned an expatriate long-term advisor and a local business development professional to complete a detailed analysis of the company and to prepare a scope of work plan for technical assistance. Each scope of work was implemented in close collaboration between our local professional staff and the client. Our local hires also monitored results and provided monthly reports detailing progress towards benchmarks and goals within the scope of work.

### b. Establishing Independent Farmers' Organizations and Modern Cooperatives

Sixty days into the Program, we completed diagnostic evaluations and interviews with more than 15 former socially owned cooperatives in the war-affected areas. In general, former socially owned cooperatives did not embrace or conform to modern cooperative principles associated with Agricultural Cooperatives in the United States and the European Union (EU). These "old-style" agricultural cooperatives operated as integrators supplying inputs such as seeds and fertilizers to individual farmers. Farmers then repaid credit in-kind with crops at harvest.

The ownership structure of these cooperatives made it difficult for them to adapt to market conditions. Low profitability, excess capacity, and over-employment characterized them. Members in the majority of these former socialist cooperatives were employees only (not farmers), and farmers had little influence on management and the type of activity undertaken. This conflict of interest resulted in poor management/farmer relationships. The participation of Croatian farmers as members in cooperatives was thus very low compared to other European countries and the United States. In 1997, Cooperatives were no longer able to effectively finance the purchasing of inputs, and the buying and marketing of grains at harvest time. Most of these former socialist cooperatives were collapsing or had already closed, and private individuals had purchased and leased their assets. The number of solvent and functioning old style cooperatives in Slavonia and Baranja rapidly declined during Phase 1 of the Program. Therefore, we concentrated resources and technical assistance on forming

new independent farmers' organizations to provide marketing and purchasing services for farmer members. It should be noted that all but one of the initial 15 "old style" cooperatives interviewed during the first two months of the Program have collapsed and are no longer operating.

c. Outreach Training for Accountants:

Throughout Phase 1, we conducted numerous seminars to facilitate the reintegration of populations in the war-affected areas. A series of seminars entitled "The Croatian Legal System and Regulations" were organized throughout UNPAs East and West. The goal of the seminars was to introduce Croatian laws to local entrepreneurs, who had been displaced or separated from Croatia during the previous six years. The seminars were facilitated in cooperation with the Croatian Association of Accountants and Bookkeepers. The seminars were attended by more than 175 participants.

d. Business Linkage Activities:

The seven-month delayed pullout of the United Nations Transitional Authority resulted in many businesses experiencing difficulty in completing trade and payment transactions outside the UN area. We approached this activity by assisting firms with obtaining information about registered bookkeepers and accountants, procedures for opening bank accounts, and information to help register in the national payment system (registration was required to complete business transactions in Croatia). In addition, we worked with individual clients to obtain used equipment, raw materials, and encouraged firms to participate in Croatian trade shows to network with potential business partners. We also worked with several commercial attaches at EU Embassies to seek foreign companies interested in investing or opening operations in Croatia. We registered clients at the Italian Chamber of Commerce in Milan and other regional Chambers, and worked closely with a parallel USAID-funded program in Bosnia and Herzegovina (BiH) providing technical assistance to SMEs.

### **C.3 Results (Phase 1)**

Summary Benchmarks and Results (Phase 1)

- 17% Annual Increase in Employment for 30 SME Clients
- 4.2% Annual Increase in Sales for 30 Assisted SME Clients
- 11 Farmers' Organizations Registered
- 295 Business (Trade) Linkages
- 52 Seminars Completed with 1,116 participants
- 27 US Volunteers Assignments
- 31 Local Consultants' Assignments Completed

We successfully met 5 out of 7 Phase 1 program targets.

a. Firm-Level Technical Assistance

During Phase 1, we designed and implemented scopes of work with more than 30 local firms. Most of these firms had fewer than 25 employees and consistently required basic marketing, strategic planning, and general business management technical assistance. Our long-term

resident expatriate advisors, local professional hires, Croatian consultants, and US volunteers recruited from our five US-based NGO/PVO partners provided technical assistance.

- Target 1.1 (15% sales growth in assisted firms) was achieved, but Target 1.2 (10% employment growth in assisted firms) was not achieved. Results were 17% and 4.2% respectively. The seven-month delayed departure of the UN from Eastern Slavonia and the introduction of significant payroll taxes in January 1998 affected employment figures. These taxes increased wage rates by more than 100 percent and caused a drop in employment levels in the short term. Businesses started recovering from this additional cost, but not before we calculated Phase 1 results;
- Target 1.3 (30 assisted firms) was achieved. We provided technical assistance to 30 clients after evaluating 122 potential companies.

b. Establishing Independent Farmers' Organizations and Modern Cooperatives:

Within 120 days, we organized 11 farmers' organizations, designed scopes of work (SoW) in collaboration with the farmers, and began providing technical assistance to implement activities detailed in the SoW. By the end of Phase I, we had organized, registered, and implemented scopes of work with 11 independent farmers' organizations.

- Target 3.1 (8 new cooperatives or farmers' organizations developed) was achieved. We organized and provided technical assistance to 11 farmers' organizations;
- Target 3.2 (10% increase in revenue of assisted cooperatives and associations) was not accomplished. Each of the 11 assisted farmers' organizations were established or (re)registered in Phase 1, but did not complete one year of business operations prior to our reporting deadlines. In addition, each of the farmers' organizations was new and, therefore, we did not have baseline data on sales until Phase 2 of the Program.
- Target 4.1 (3000 benefiting members in farmers' organizations) was accomplished. The total membership in the 11 farmers' organizations was more than 3,750.

c. Outreach Training for Accountants:

Our training and technical assistance for clients in the former UNPAs assisted 79 companies in successfully adjusting to the new tax regulations that became effective in January 1998. Each of these assisted companies established a new accounting system and filed its first quarterly financial statement at tax offices in Croatia.

d. Business Linkage Activities:

We assisted more than 40 companies in the former United Nations Transitional Area of Eastern Slavonia (UNTAES) in adjusting to the loss of markets in the Federal Republics of Yugoslavia (FRY) by creating 295 new business linkages, as they attempted to penetrate markets in other parts of Croatia and abroad.

- Target 2.1 (150 transactions linking enterprises in formerly occupied regions to Croatia and abroad) was accomplished. We completed more than 295 linkages between companies in the war-affected areas and other parts of Croatia and abroad.

## **D. PHASE 2 ACTIVITIES AND RESULTS (December 1998 to December 1999)**

### **D.1 Strategy and Program Implementation (Phase 2)**

At the beginning of this phase, USAID requested that we realign our targets and indicators (see chart 2 below).

During Phase 2, we expanded activities to include former UNPAs North and South. Based on experience and results from Phase 1 activities, we increased our activities with farmers in the war-affected areas. Activity during Phase 2 included a rapid assessment and start-up for new offices in former UNPAs North and South. Offices in Petrinja (former Sector North) and Knin (former Sector South) were opened in November 1998.

As noted above, we concentrated greater effort on assisting farmers' organization in Phase 2. In sectors North and South, strengthening the primary agricultural sectors and providing technical assistance to farmers through farmers' organizations represented the best opportunity for increasing household income within a short time period. This was also true in the other two war-affected areas (East and West).

A significant slowdown in the Croatian economy began in November 1997 and continued through Phase 2. This slowdown impacted the war-affected areas just as most companies were adjusting to new tax and regulatory issues, and as returnees were beginning to settle in these areas. Increasing liquidity problems within the local commercial banking sector made debt financing, already difficult to secure, virtually unavailable to the SME sector. Foreign banks were also reluctant to lend in the war-affected areas, especially within the agricultural sector.

The local interest in organizing farmers' organizations and modern agricultural cooperatives increased throughout Phase 2. Despite the consolidation of some smaller farmers' organizations and the failure of others, we continued to actively support eleven farmers' organizations and added one business association to our portfolio. Total membership in these organizations exceeded 3,700 members. While the problems with the economy discussed above impacted total sales and employment, they actually encouraged an increase in membership within these organizations as potential members observed the benefits and results of organized marketing and advocacy initiatives.

Our regional offices reported that most clients still faced challenges accessing capital, which slowed the potential growth rate for SME clients. Ministry of Reconstruction and Development (HBOR) loans were not disbursed, and short-term interest rates increased to 19-25 percent. Poor liquidity in the economy continued to be a fundamental problem affecting all clients throughout the war-affected areas, except those who primarily exported. We also documented increasing receivables for most clients (except for export-oriented SME clients). Receivables among our clients in Phase 2 increased by more than 150 percent compared to Phase 1 and exceeded USD 5.5 million by November 1998. Poor liquidity and weakening domestic demand for products also limited expansion by those clients that had limited export potential.

**Chart No. 2: (Phase 2 Strategic Framework, Indicators, and Targets) USAID/Croatia Strategic Objective (SO) 1:**  
Reintegration of War-Affected Populations

**Intermediate Result (I.R.) 1.1**

**War-Affected Populations Become Economically  
Productive Members of Society**

**I.R.1.1.1:**

Enterprise Growth  
and Expansion

**Indicator:** Number of  
assisted client firms

**Target:** 60

**Indicator:** Sales growth  
in client firms

**Target:** 15%

**Indicator:** Employment  
growth in client firms

**Target:** 10%

**I.R.1.1.2:**

Reintegration of  
Regional Economies

**Indicator:** Number of  
linkages connecting firms  
in war-affected areas to  
other parts of Croatia

**Target:** 150

**I.R.1.1.3:**

Agricultural Cooperatives  
and Associations  
Developed

**Indicator:** Number of new  
coops or associations  
developed

**Target:** 8

**Indicator:** Increase in  
membership and non-member  
contract farmers

**Target:** 25%

**Indicator:** Increase in sales  
for assisted agricultural  
cooperatives and associations

**Target:** 10%

**I.R.1.1.4:**

Membership in Assisted Industry  
Associations

**Indicator:** Total number of members of  
assisted associations

**Target:** 12,000

## **D.2 Program Components (Phase 2)**

To implement and accomplish Phase 2 strategy and goals, our activities were organized into four program components:

- Firm-Level Technical Assistance;
- Technical Assistance to strengthen Farmers' Organizations;
- Industry Association Development Activities;
- Regional Trade Activities.

### a. Firm Level Assistance

During Phase 2, we expanded our active client base to 60 firms. We continued providing technical assistance and training at the firm level through a variety of vehicles and methods, including:

- One-on-one consulting and information services at our five Business Advisory Centers;
- Local consultant assignments;
- Local professional personnel assignments;
- Long-term resident expatriate advisors;
- US volunteer advisors and consultants.

### b. Technical Assistance to strengthen Farmers' Organizations

Prior to the conflict in Croatia, private farming was a secondary source of income for most households. With the collapse of the rural economy within the war-affected areas, private farming became the primary source of income for most households.

We continued to provide technical assistance to 11 farmers' organizations that were organized and registered during Phase 1. Membership increased to 3,700 and our technical assistance concentrated on marketing assistance, production scheduling, and budgeting. In many cases, farmers were returning after living for more than 4 years in BiH or FRY, and market realities had changed significantly. Many returnee farmers in Former Sectors West, South, and North sold products to Yugoslavia and the Republika Srpska (RS) in BiH during the Krajina period and these markets had collapsed over the prior 3 years. We assisted farmers with locating new markets but had limited success obtaining debt financing. Each of our regional offices reported that lack of start-up financing remained an obstacle to returnees and to restructuring production for new markets. For example, farm equipment, buildings and livestock were lost or destroyed during the conflicts, and the limited access to financing to replace livestock and equipment hampered our efforts to increase the production of quality products.

### c. Industry Association Development Activities

We started providing technical assistance to an association of small and medium- sized enterprises as part of a strategy to improve the operating environment in Croatia for SMEs. The Small and Medium- Sized Enterprise Association (SMEA) was prior to our assistance, a part (sub group) within the Croatia Employers Association (HUP). In December 1997, prior

to registering as an independent association, members voted to establish an independent advocacy association because their primary concerns were not on the agenda within HUP.

#### d. Regional Trade Activities

At the beginning of Phase 2, recognizing the importance of trade and exporting to the future growth of our SME clients, we allocated more resources to developing trade and business between companies in the war-affected areas, as well as other parts of Croatia, and foreign markets.

We provided a variety of technical assistance and information for our clients and foreign companies interested in conducting trade and business in Croatia. These services and information included:

- Market research;
- Due diligence on trade leads and contracts;
- Investment promotion;
- Access to a network of partner organizations in surrounding countries (Romania, Bulgaria, Macedonia, Albania, and Montenegro) offering similar services and information.

### **D.3 Results (Phase 2)**

#### Summary Benchmarks and Results (Phase 2)

- 20% Increase in Employment for 60 SME Clients
- 17% Increase in Sales for 60 SME Clients
- 7 Farmers' Organizations transformed into Modern Agricultural Cooperatives
- 16 Farmers' Organizations Registered
- 500 New Members in Client Farmers' Organizations and Modern Agricultural Cooperatives
- 276 New Business (Trade) Linkages
- 58 Seminars Completed with 1,116 participants
- 34 US Volunteers Assignments
- 43 Local Consultants' Assignments Completed

#### a. Firm-Level Technical Assistance

More than 160 private businesses were provided technical assistance and training during Phase 2. Of these, we designed and implemented scopes of work with 60 firms. These companies reported, on average, a 20% increase in employment (470) and a 17% increase in sales during Phase 2. Our SME clients continued to outperform the overall economy. The Croatian economy continued to struggle and recorded 5 consecutive quarters of recession. GDP decreased by 0.8 percent during this period and industrial production showed no signs of recovery. At the end of December 1999, industrial production had declined by 1 percent compared to the corresponding period in 1998.<sup>2</sup> In December 1999, registered unemployment in Croatia was 20.4 percent, which was a 12.9 percent increase compared to

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<sup>2</sup> Croatian National Bank, Bulletin No. 45, January 2000

December 1998. In addition to rising unemployment, there were still an estimated 150,000 employed workers who were not paid regularly.

During this phase, we completed 34 US volunteer and consultant assignments, 43 assignments with local consultants, and 58 seminars with 1,116 participants. During Phase 2, clients received technical assistance from resident expatriate advisors, local professional personnel, local consultants, and US volunteer advisors, that included more than 1,540 hours of hands-on consultation and training.

#### b. Firm-Level Technical Assistance to Strengthen Farmers' Organizations

In Phase 2, we expanded our grass roots campaign to organize and register farmers' organizations in the war-affected areas, and to focus on marketing assistance, production scheduling, and budgeting. This effort was a success. We organized and registered 16 new farmers' organizations during Phase 2 and provided on-going technical assistance to 27 farmers' organizations, including 7 modern agricultural cooperatives. During this phase, we also focused technical assistance on strengthening farmers' organizations to expand membership and ensure sustainability. Membership increased from roughly 3,700 to 7,400, including more than 500 new returnee members.

Toward the end of Phase 2, we focused fewer resources on registering farmers' organizations and concentrated more resources on transforming existing organizations into modern agricultural cooperatives. For these cooperatives, we provided a broad range of technical assistance focusing on marketing assistance, production scheduling, budgeting, and accounting.

At the conclusion of this phase, we began preparing policies and procedures to implement a new grant fund to capitalize agricultural cooperatives and associations. The new grant fund was incorporated into the existing Cooperative Agreement under modification 06, which was signed by the USAID Agreement Officer on December 3, 1999. The goal of the grant fund was to provide support for refugees and displaced persons using innovative funding strategies for economic development projects targeting modern cooperatives. The objective was to leverage technical assistance with grant funds to promote economic development and income generation due to the lack of availability of commercial debt financing for farmers.

#### c. Industry Association Development Activities

As anticipated at the beginning of Phase 2, our regional and national industry association development activities were the most challenging aspect of the program. SMEA and the Union of Associations of Farmers in Slavonia and Baranja (UNION) were identified as clients and received technical assistance during Phase 2. Both organizations expanded membership by about 10 percent, but added few new services for members and were not successful with promoting policy reform agendas.

The purpose of these activities was to create an enabling environment conducive to private sector development. The enabling environment in Croatia did not improve in this phase. There was limited political commitment by either local or national governments to support private business, the legal system remained politicized, laws were not enforced, property rights were not protected, and the tax system was overly burdensome. There also remained

very few independent industry associations representing and promoting private sector interests.

SMEA and the UNION were both private organizations registered to represent private sector interests. It became apparent during Phase 2 that these organizations did not have the organizational vision and institutional capacity to promote reform. Our technical assistance concentrated on developing and drafting policy reforms, and strengthening the associations by adding more services for members. US advisors provided technical assistance in the following areas:

- Training an effective Management Board;
- Identifying leaders and improving leadership skills;
- Improving organizational and staff capacity;
- Improving clients' reputation for competence;
- Implementing "value-added" services for members;
- Preparing effective business plan and management practices;
- Improving fund raising skills;
- Improving marketing capacity and good media relations.

#### d. Regional Trade Activities

We continued to promote exports and business linkages and successfully facilitated 276 transactions for our clients to expand exports and domestic sales in non-traditional markets. We continued to target Croatia's largest export market, the EU, and traditional markets in the region. Promoting exports reduced the effect of weak domestic demand and avoided increasing receivables caused by large inter-company arrears in Croatia.

We completed numerous activities to build these exports and business linkages. A trade database was created and our local professional personnel actively updated the database weekly and utilized the contact information and leads to pursue linkages for our business clients. These activities were interconnected with both our firm-level assistance and agricultural association and cooperative assistance programs. Each office also distributed trade leads to other offices in weekly reports. Our marketing database included company information on more than 180 Croatian companies and foreign companies pursuing business opportunities in the war-affected areas or which had expressed an interest in operating in these regions.

During this phase we also joined a new USAID Office of Business Development initiative to expand a new electronic commerce system, Global Technology Network (GTN), into Croatia. GTN targeted small and medium-sized enterprises seeking access to US and regional markets. GTN partners in Macedonia, Bulgaria and Romania were linked together through an internet-based communications and trade lead system that facilitated collaboration throughout the region.

### **E. PHASE 3 ACTIVITIES AND RESULTS (January 2000 to April 2001)**

#### **E.1 Strategy and Program Implementation (Phase 3)**

As anticipated at the beginning of Phase 3, our highest priority for the Program was to incorporate a grant component into our existing technical assistance program for farmers'

organizations, and to come to an agreement with USAID on the policies and procedures for the new grant program. A verbal agreement was reached for the policies and procedures in mid-February 2000, and written approval for the policies and procedures was provided in June 2000.

During this phase, we continued to provide a broad range of services and technical assistance to SMEs and agricultural cooperatives exclusively in the war-affected areas of Croatia. The program slightly shifted resources toward agricultural development projects and trade activities with the introduction of the new grant fund to capitalize agricultural cooperatives and the introduction of an electronic commerce system to augment regional trade activities. The fundamental objective of the Program remained the strengthening of private SMEs and farmers' organizations to facilitate the reintegration of the war-affected populations of Croatia.

In the final four months of the Program, we concentrated resources on completing ongoing grant projects with partner organizations and clients, and completing business plans and annual production plans for farmers' organizations. In addition, we completed six municipal surveys and concept papers for USAID "partnership municipalities."

A USAID review team completed a two-week assessment of the Program on September 22, 2000. The decision not to extend or modify the current program beyond April 2001 was based on the development of a new strategic framework at the USAID/Mission in Zagreb.

**Chart N. 3 (Phase 3 Strategic Framework, Indicators, and Results): USAID/Croatia Strategic Objective (SO)1:**  
Reintegration of War-Affected Populations

**Intermediate Result (I.R.) 1.1**

**Economy strengthened to create opportunities for affected populations**

**I.R.1.1.1:**

Enterprise Growth and Expansion

**Indicator:** Number of assisted firms

**Target:** 335

**Indicator:** Sales growth in client firms

**Target:** 15%

**Indicator:** Employment growth in client firms

**Target:** 10%

**I.R.1.1.2:**

Reintegration of Regional Economies

**Indicator:** Number of linkages connecting firms in war-affected areas to other parts of Croatia

**Target:** 160

**Indicator:** Number of linkages connecting firms in war-affected areas to international markets

**Target:** 80

**I.R.1.1.3:**

Agricultural Cooperatives and Associations Strengthened

**Indicator:** Number of new coops or associations developed

**Target:** 11

**Indicator:** Increase in membership and non-member contract farmers

**Target:** 25%

**Indicator:** Increase in sales for assisted agricultural cooperatives and associations

**Target:** 15%

**I.R.1.1.4:**

Registering, strengthening and training industry associations to address policy and regulatory issues

**Indicator:** Number of new regional and national associations

**Target:** 4

**Indicator:** Increase in dues-paying membership (percentage of membership)

**Target:** 75%

**Indicator:** Total number of members of assisted associations

**Target:** 12,000

**Indicator:** Policy and regulatory issues identified and solutions proposed and submitted

**Target:** 4

## **E.2 Program Components (Phase 3)**

To implement and accomplish the strategy and goals, our activities were organized into four core program components:

- Firm-Level Technical Assistance;
- Agricultural Cooperative Development;
- Regional Trade Facilitation;
- Local Economic Development Grant Projects.

### a. Firm-Level Technical Assistance

Firm Level Technical Assistance remained an integral component of the Program during all three phases. Phase 3 firm level technical assistance concentrated on four areas: financial management, operations management, and marketing management, and also improving access to capital by preparing business plans. As in the previous phases, a variety of vehicles were used to work with companies, such as one-on-one consulting from resident expatriate advisors, local consultants and local staff, and seminar and work shop training for larger groups.

We continued to provide training and technical assistance to 60 active business clients and retained our goal of increasing sales by 15 percent and employment by 10 percent for each of these client firms. In addition, training seminars and technical assistance were planned for 285 additional businesses during Phase 3. The total number of businesses receiving training was expected to exceed 326.

### Financial Management Training and Technical Assistance

Financial management training and technical assistance was accomplished in several ways. First, firms were provided assistance in implementing sound accounting practices. Through direct assistance to management, we assisted firms in the principles of accountability, transparency and compliance to provide them with additional tools for oversight of their firms, a flatter management structure and a firm legal footing. We partnered with local certified accounting firms and associations, provided training, where necessary, for the accountants and the firms, and facilitated relationship building between these organizations for the future development of each.

### Operations Management

Operations management consisted of, primarily, the support of US volunteer executives to implement training in production and logistics management. Volunteer executives helped firms to develop their supply chains, efficiencies, distribution and transportation structures to allow firms to compete with local and international firms, and provide better partnering opportunities for foreign businesses. We directly assisted by continuing to update our database of suppliers and partners to enable client firms to develop their business opportunities.

## Marketing Assistance and Marketing Management

Marketing assistance and marketing management were implemented through the development of marketing surveys with support from volunteer executives and local consultants. Further marketing development occurred through foreign partnering. Once firms became viable in terms of core management (finance and operations), they were better prepared to bring products to market. Foreign partners and marketing surveys provided this knowledge and enabled assisted firms to increase revenues, decrease receivables and establish products in markets unknown or unavailable to them at the time.

## Improving Access to Capital

As firms became more capable at managing products and assets, they were better positioned to develop relationships with sources of commercial finance and to receive commercial financing for future growth and expansion. We continued to update our existing database of financing sources and developed relationships with these financial institutions. As assisted firms developed, the relationship between FLAG and these financial institutions facilitated client access to capital, allowed relationships to develop between the institutions and the firms, and helped both grow. There is still a dependence on subsidized financing and grants within the SME community. However, these sources have proven unreliable, politicized and not sustainable sources of capital for the long term.

## Impact and Sustainability

The broad range of services provided by FLAG required partnering with several domestic institutions to jointly conduct training. Our strategy for the sustainability of firm-level assistance (technical and management training for SMEs) included two complementary types of activities to achieve impact. First, by providing direct assistance to SME owners and managers, our business clients were trained and continue to apply the new concepts and approaches. Second, by “training the trainers” of local partner institutions, developing seminar material and a fee-for-service component in conjunction with these partners, we had a long-term impact on the local institutions’ ability to champion these new concepts. These local partners continue to disseminate the new concepts to a broader audience throughout Croatia.

### b. Agricultural Cooperative Development

Based upon the success of the past 47 months and its immediate impact on return, Phase 3 activities concentrated the largest percentage of resources and technical assistance on strengthening agricultural cooperatives and associations. We added 5 additional cooperative clients to our existing 7 in the portfolio, and added 6 additional agricultural association clients to the existing 27 in the portfolio.

### c. Regional Trade Facilitation

Facilitating linkages and trade between companies in the war-affected areas, as well as other parts of Croatia, and foreign markets required increased resources from local professional staff at our main office. Therefore, one local professional hire was assigned to coordinate all trade activities and training.

In Phase 3, we facilitated linkages between companies in the war-affected areas and other parts of Croatia, and between companies in the war-affected areas and international markets.

To accomplish this, CY2000 trade facilitation activities consisted of three areas:

- Global Technology Network (GTN);
- FLAG Marketing Database;
- Training and Technical Assistance

#### Global Technology Network (GTN)

The Global Technology Network (GTN) assisted Croatian small and medium-sized firms seeking access to US and regional markets. GTN partners in Macedonia, Bulgaria and Romania were linked with an internet-based communications and trade lead system that facilitated collaboration throughout the region. GTN was operated by USAID's Office of Business Development and FLAG was the initial local partner for the GTN system in Croatia.

The GTN Croatia database contained 150 Croatian companies in the war-affected areas. We regularly updated the existing company information, which was completed in January 2000. We then began marketing the system to other companies in the war-affected areas in February 2000. The goal was to increase the number of companies in the database from 150 to 300, and this goal was achieved.

#### FLAG Marketing Database

FLAG's marketing database for clients in the war-affected areas included company information from Croatian companies and foreign companies operating or who had expressed interest in operating in these areas. We continued to maintain and regularly update the database during Phase 3.

#### Trade Facilitation Training

Based on lessons learned, we provided training and technical assistance for entrepreneurs to help prepare SMEs in all aspects of exporting. Assistance included information on identifying markets, developing market entry strategies, responding to inquiries, creating advertising strategies, developing trade leads, preparing export documents, transporting and delivering goods, and getting paid.

#### d. Economic Development Grant Projects

A new sub-component of our agricultural cooperative and association-strengthening project was a USD 800,000 grant fund to capitalize existing clients. Policies and procedures for the grant program were submitted simultaneously with our CY2000 work plan for review and approval by USAID/Zagreb. The policies and procedures were developed in order to insure a careful, deliberate design process and to ensure a rapid execution of the grant projects. Our goal was also to leverage the grant fund with contributions from other donors, processors and the farmers. The goal was to increase the fund by 25% with additional funding from other sources.

### **E.3 Results (Phase 3)**

#### Summary Activities and Results (Phase 3)

- 10% Increase in Employment for 60 SME Clients
- 18% Increase in Sales for 60 SME Clients
- 5 Farmers' Organizations transformed into Modern Agricultural Cooperatives
- 11 Farmers' Organizations and Industry Associations Registered
- 660 New Members in Client Farmers' Organizations and Modern Agricultural Cooperatives
- 295 New Business (Trade) Linkages
- 52 Seminars Completed with 1,116 participants
- 32 US Volunteers Assignments
- 41 Local Consultants' Assignments Completed
- 12 Economic Development Grant Projects Completed
- 6 Municipal Economic Surveys Completed

#### a. Firm-Level Technical Assistance

SME clients in the war-affected areas continued to outperform the overall economy with sales increasing by 10 percent. The Croatian economy continued experiencing modest improvements and the government began following through with an austerity plan that included allowing insolvent companies to enter bankruptcy. Although the unemployment figures increased, there was an increase in available capital and inter-company arrears declined.

We completed 19 business plans, 9 market surveys, 9 feasibility studies, 11 volunteer assignments, 11 local consultant assignments and 15 seminars for business clients in Phase 3.

#### b. Agricultural Cooperative Development

We assisted in the transformation of five agricultural associations into 5 new agricultural cooperatives, and also organized 6 new agricultural associations. We provided assistance to 41 agricultural cooperative and association clients. We focused technical assistance on strengthening existing association and cooperative clients to ensure sustainability. Membership in agricultural cooperative and association clients increased by 950 new members.

In the second half of Phase 3, we intensified work with agricultural associations and cooperatives in new “partnership municipalities” identified by USAID. Our focus was on completing ongoing grant projects, providing advice on marketing, production scheduling, budgeting, and accounting to association and cooperative clients in order to ensure their sustainability and strengthen their organizational infrastructure to make available more services to existing members.

Our technical assistance concentrated on institution building, impact, and sustainability. To achieve this goal, 12 market surveys, 12 feasibility studies, and 23 seminars were completed during Phase 3. In addition, 25 US volunteers and 25 local consultants were recruited for projects.

As a part of technical assistance for both SME and association/cooperative clients, we continued organizing in-country training. We completed 55 training events with 1,340 participants of whom 9% were female.

Also, as a part of the Cooperative Leaders TRANSIT program organized by World Learning, six client managers traveled to the US for training. These six individuals managed associations and cooperatives in the war-affected areas. The USAID-sponsored two-week training program in the US included visits to sugar beet and dairy cooperatives, to research farms, meetings with the members of farmers unions, and a session with a USDA Inspector. The implementing organization was the Montana State University of Bozeman, Montana.

#### c. Regional Trade Facilitation

We continued assisting our clients in activities related to exports and business linkages. We facilitated 295 new business linkages for our clients helping them to increase export and domestic sales in non-traditional markets.

#### d. Economic Development Grant Projects

Our regional offices completed and submitted 37 initial evaluations and 23 final grant project proposals. Twelve of these 23 projects were approved for funding and were implemented. A summary of each approved project is included as attachment C. These 12 projects equal an approved allocation of USD 810,083 and were coordinated with donations and low-interest loans from other donor organizations (USD 281,000).

### **F. LESSONS LEARNED AND RECOMMENDATIONS**

The past 47 months provided an opportunity to identify ways in which the original Program could be strengthened to facilitate the reintegration of the war-affected populations. Many of the issues discussed below have been presented to USAID in quarterly reports during the life of the Program, or discussed at USAID planning meetings. This section attempts to provide not only lessons learned but also recommendations for continued assistance to SMEs and farmers' organizations in the war-affected areas of Croatia. As such, this section is strongly integrated with Section E, which details activities in the final phase of the project.

#### **F.1 Management Lessons and Recommendations**

Sustainability of our technical assistance services was not an issue of primary concern at the beginning of the project in 1997. Instead, the program's broader systemic impact on the return of populations and reintegration of the war-affected areas was the primary concern. In modification 06, we began shifting emphasis toward building sustainability for our services, and the sustainability of local business support organizations and partner institutions into the design of the program. After reviewing an extensive list of local partner institutions involved with training over the past 47 months, we have identified several partner institutions that should continue to receive training and technical assistance in the future, including the Independent Association Of Agricultural Cooperatives. We have conducted seminars and training in cooperation with many of these local institutions, but have not provided technical assistance to strengthen these institutions. They are each worthy candidates for continued assistance under the new NGO Strengthening Program. It is worth noting that many of these

local partners not only provide training and services in the war-affected areas, but also provide training and services throughout the country. Many have main offices in Zagreb and rely on service fees and membership dues to cover operating costs. Several also continue to rely on donor and government funding.

We have noted an increased interest among foreign donors to concentrate on economic development and to provide business support programs in the war-affected areas. This was a welcome relief from the past, when most organizations concentrated resources on rebuilding infrastructure and providing emergency relief donations in the war-affected areas. Since coordination among the other donors providing economic development assistance in the war-affected areas was always very limited, we unilaterally contacted foreign embassies and other donor organizations to coordinate activities. This method proved only marginally beneficial as most organizations had separate priorities and there was no mechanism in place to coordinate assistance. Future donor programs need to be coordinated closely with local communities to leverage resources, limit duplication of activities, and maximize the coordination of economic development activities in each region.

Located in geographically diverse regions throughout Croatia that are facing distinct sets of economic and reintegration challenges, our four regional offices were provided autonomy and treated independently in order to devise relevant solutions locally to address particular problems in the region. Several difficulties and benefits emerged with this approach. First, SMEs throughout Croatia are demanding similar business support services and training. We were able to use standard training seminar formats in each office to address the training needs when demand was consistent across regions. Second, local professional personnel in each office had unique business backgrounds and experience. Towards the end of the Program, we were able to capture the diversity of the local professional skills in regional offices and used them more effectively throughout each region. We implemented a project-wide approach to leverage experience, training programs, and local professional personnel among all the offices.

## **F.2 Firm-Level Assistance Lessons and Recommendations**

The past 47 months of providing technical assistance to SME clients has revealed a strong interest among clients in four key areas: financial management, operations management, marketing and marketing management, and improved access to capital. Since clients have demanded more technical assistance in these areas, the final phase of the program concentrated on these areas.

We experienced challenges and even difficulty following up on such a large number of business clients in these areas receiving one-on-one technical assistance and consulting from US volunteers and the resident expatriate personnel. Given the small number of personnel involved and the large number of companies demanding these services, we reduced the number of active business clients and conducted more targeted seminar training to a broader audience of managers and owners. The result was continued high-quality assistance to clients that demonstrated a potential for creating jobs and training for a larger number of managers and owners that would otherwise not receive such assistance. Start-up companies and SMEs in the war-affected areas tend to employ relatively small numbers (less than 20). The cost/benefit of one-on-one consulting for companies with few employees has shown moderate results in terms of creating jobs. The goal of expanding seminar and outreach

training to a larger audience is to create jobs at a higher rate by broadening the impact of the training and technical assistance program.

Achieving sustainability for our business services in the war-affected areas was a difficult but necessary objective. Over the 47 months, we did not implement a fee-for-service component because of the poor economic conditions resulting from the recent conflict and transition to a market economy. The geographical limitation of working only in the war-affected areas also limited the likelihood of working with companies capable of paying fees for business services. At the beginning of Phase 3, we designed a fee-for-service component for some of our services (mainly marketing and business planning activities). This fee-for-service component did not cover operating costs for these services, since many of the companies were unable to afford the substantial fees associated with local professional business services. In addition, many SMEs did not, at that time, value many of these services. In the war-affected areas, continued donor support will be necessary to continue providing services to these smaller companies.

Our fee-for-service component was coordinated with local partner institutions to improve their financial sustainability and the sustainability of their services. At the conclusion of our program, there was not a single business support service organization operating in the war-affected areas capable of providing the broad range of services offered by FLAG. Therefore, efforts to develop fee-for-services with local partner organizations should be diversified and local organizations operating outside the war-affected areas should be targeted as partners to provide these services. Many of the potential domestic partners operate countrywide and are capable of, and mainly interested in, providing similar training and services to companies throughout Croatia, not only the war-affected areas. These potential domestic partners do not view the war-affected areas as a separate part of Croatia and provide services where demand is highest and where companies are capable of paying fees. It has been a challenge to identify local institutions within the war-affected areas capable of providing services.

We continued provide training to local professional personnel and local consultants to improve their expertise and ability to continue providing these services at the conclusion of our program. Training for local professional personnel and consultants focused on business planning, financial management, and marketing. At the conclusion of the program, we assisted several local personnel to register a limited liability company to continue providing similar services to companies within and outside the war-affected areas. To illustrate our commitment to these local personnel and to Croatia, we would like to highlight that we have maintained our presence in Croatia following the end of the program in April 2001. By August of 2001, our local personnel and our own investment in developing the private sector in the war-affected areas will total over \$60,000 in direct expenses. We believe this demonstrates our resolve to continue providing professional business services after the life of donor funding.

### **F.3 Agricultural Cooperatives and Farmers' Organizations Lessons and Recommendations**

One of the more resource intensive activities in our program is providing technical assistance to farmers' organizations. Additional personnel supported our communication and planning among regional offices in Phase 3 to collect and disburse research and monitor results across the country. Regional Directors and local agricultural advisors based in different geographical areas tended to rely on their own research and local professional personnel were

involved with more monitoring and less technical assistance as the program expanded. In addition, local agricultural advisors were unable to specialize and concentrate on providing technical assistance in key areas of expertise as they dedicated more and more time to monitoring activities. As a result, there was duplication in several areas such as market research and project design, and agricultural advisors were not utilized effectively in their areas of expertise. To overcome these difficulties, we implemented a weekly reporting system by each regional office to specifically disseminate research and market information and hired a resident expatriate agricultural advisor to manage project development and technical assistance. The new advisor managed the placement of local advisors and assisted with designing scopes of work for agricultural technical assistance projects. In Phase 3, local agricultural advisors and professional staff were available across geographical areas and specialized in key areas, such as livestock, vegetables, dairy, and an effective communication structure was established. All key documents related to farmers' organizations were also available for regional offices on our central web-based electronic library and Dbase. As a result, we were able to successfully register and provide technical assistance to 38 farmers' organizations with the same personnel who registered and provided technical assistance to 14 farmers' organizations in Phase 2.

Many of these farmers' organizations initially represented a variety of producers such as grain and livestock producers, had limited access to capital and required full-time management to succeed. There was a conflict of interest between the grain producers and livestock producers and the continued reliance on mixed production did not allow the producer members to have the economies of scale to survive. Specialization and expansion was the key to survival for these small farmers.

Based on these circumstances, we initiated two strategies. First, several farmers' organizations were transformed into specialized agricultural cooperatives. The specialized cooperatives required a larger membership fee and were initially smaller in membership compared to the parent associations. The demand for specialized cooperatives increased as farmers realized the benefits of specializing and joint marketing and purchasing activities. Second, we requested funding from USAID to capitalize some of these new cooperatives and associations. Our grant program was a result of the limited access to capital and bias against lending to agricultural producers by the commercial banking sector. The grant program was a success in that we quickly generated income for farmer members, created sustainable cooperatives with revolving credit funds and increased production to a level that interested processors to sign forward contracts. Despite the success, the grant program was an emergency response to an economic crisis and did not change the fundamental challenges facing farmers, which includes limited access to debt financing. An alternative solution to this problem such as an inventory credit and other alternative financing programs should be implemented to resolve the fundamental issue.

The impact of these farmers' organizations on return and reintegration was substantial, since the majority of returnees are in agricultural areas and have experience in agriculture. We allocated the largest percentage of our resources to this program component in Phase 3 because of the potential for having an immediate impact on generating income for returnees. It should be noted however, that the number of farmers is expected to decrease as the more efficient farmers expand and others cannot compete. In the long term, alternative employment opportunities other than primary agricultural production need to be created by the SME sector in the war-affected areas. Agricultural programs are not the panacea for resolving the employment problems in the war-affected areas.

In the past 47 months, more than 30 cooperative managers and representatives of the local Agricultural Extension service have participated in World Learning organized TRANSIT programs. The TRANSIT programs were designed to build leadership skills among participating managers and to train extension agents in cooperative organization and leadership. We continued to informally cooperate with the local agriculture extension service in each region and conducted numerous seminars in conjunction with the service. The extension service has also assisted with registering cooperatives and provided technical assistance to our clients. We recommend for future donor programs to leverage the existing skills and resources within the Extension Service to provide sustainable services to farmers and cooperatives. Our agricultural technical assistance services and program were partially coordinated through such local institutions, such as the Croatian Extension Service and local Agricultural Faculty at Universities in Osijek, Zagreb, and Split. Building the capacity of local institutions to continue providing these services should be a priority for future programs. (Please see Attachment – B for a complete description about our best practices in Croatian agricultural cooperative development).

#### **F.4 Regional and National Industry Associations Lessons**

The purpose of our activities with regional and national industry associations was to create an enabling environment conducive to private sector development, which was a precondition for leveraging our business development services. The enabling environment in Croatia over the past 47 months modestly improved in Phase 3. In Phases 1 and 2, there was no political commitment by either local or national authorities to support private business, the legal framework was politicized, laws were not enforced, property rights were not protected, the tax system was overly burdensome, and there were limited institutions (government and non government) representing private sector interests.

After 47 months of activities, it is apparent that the enabling environment cannot improve without more substantial involvement by independent industry associations participating in the reform process. However, the existing associations do not yet have the organizational vision and institutional capacity to promote reform. Our technical assistance concentrated on developing and drafting policy reforms and institutional strengthening for two such associations. Our consultants provided technical assistance in drafting policy reform. The associations adopted policy reform platforms and recommendations were submitted to the appropriate authorities. Despite this success, no policy reform recommendations from these associations were implemented. At the same time, we provided technical assistance on institution building and adding new services for members. However, relatively few new services have been developed and membership in these associations is stagnant.

Two suggestions are proposed for future programs. We relied too heavily on US advisors to draft policy reform, which had a negative result because many Croatian advisors felt that the policy model resembled a US solution to a Croatian issue. To overcome this effect, we included more local advisors along with the US advisors to draft policy reform. The result was positive as more policy recommendations moved forward without substantial delays within the associations. Second, additional work is needed to consolidate geographically disparate agricultural associations with overlapping functions and advocacy efforts at both the local and national levels. We recommend technical assistance to begin merging the services and advocacy services from the groups into regional associations representing

specific agricultural industries. In the current environment, the government and industry can easily “divide and conquer” the farmers.

### **F.5 Trade Facilitation and Linkages Lessons**

Facilitating trade linkages for clients in the war-affected areas was a complex challenge for two primary reasons. First, there was limited information available to SMEs about trade opportunities. Second, many SME clients did not traditionally export and did not have the in-house skills available to conduct market research, to prepare export pricing and quotes, or to research the lowest cost freight forwarders, insurance agencies, and transport companies.

We noted an increased demand for trade related services during Phase 3 as companies continued to search for export markets due to the liquidity problem in the Croatian economy. Many companies were also beginning to revive former contacts in the Southeast Europe region. One of the lessons learned early in the program was the need to collect trade leads from each regional office, document the information in a database and distribute the lead to our regional offices. This simple technique resulted in more completed business transactions than any other method. We created a simple marketing database that includes contact information for both foreign and Croatian companies buying and selling in the war-affected areas. We eventually dedicated a full-time local professional to collect and disseminate trade leads to our offices in the region. Based on our surveys of clients at the end of the program, this service has the most potential for generating fees for local advisory and business support programs.

**BEST PRACTICES IN CROATIAN AGRICULTURAL  
COOPERATIVE DEVELOPMENT**



FLAG International, LLC  
Annapolis, Maryland

April 2001

## **EXECUTIVE SUMMARY**

The focus of this paper is to summarize methodologies used in forming and strengthening farmers' associations and cooperatives in the war-affected areas of Croatia, and to recommend best practices for donors and organizations providing support to these organizations. Due to the importance of agriculture in developing Croatia's war-affected economy, thereby promoting the return of displaced populations, we encourage any future donor organizations working with this sector to follow the recommendations highlighted below as they have proved successful in the past three years. Given the potential size of this economy, however, there is still a long way to go. As the potential is developed and the region is more integrated with Croatia's economy, and that of the region, the methodology will change. At this point, though, the following recommendations still point to the best route for encouraging economic recovery.

Family farms are the foundation of Croatian production agriculture. These farms account for 80 percent of the agricultural land, 90 percent of the tractors, 90 percent of the agricultural workforce, and 45 percent of the Croatian population. In 2000, there were 600,000 private family farms, of which 9 percent offered full-time employment to at least one family member. However, these farms are small and fragmented (averaging 2.8 hectares on 8 plots). During the socialist era, agricultural enterprises (agro-kombinats and socially owned cooperatives) employed 40,000 and produced 35 percent of all agricultural products and dominated the agricultural processing sector and livestock trade. These enterprises were primarily responsible for integrating the small family farms into agricultural markets and in supplying them with inputs and services. Yet, with the introduction of a market economy, these enterprises have collapsed at an alarming rate during the past decade and are no longer reliable partners for small private farmers.

The following 31 recommendations are based on three years of working directly with farmers, farmer associations and cooperatives, and businesses involved in both the upstream and downstream activities related to these agricultural enterprises. Further recommendations have been summarized from work with US-based volunteers who assisted implementation of development work in the agriculture sectors of war-affected regions in Croatia. While not necessarily presented as a chronological methodology they highlight the steps necessary to successful cooperative development, key training issues for members, leaders and managers, and follow up advice necessary to sustainable operation of a modern, successful farmer cooperative in war-affected regions of Croatia.

## **INTRODUCTION**

With liberalization in 1992, private entrepreneurs, trading companies, and newly privatized cooperatives quickly replaced the socially owned enterprises and cooperatives in providing inputs (mostly offered through government programs), and providing alternative marketing channels to small farmers. These private entrepreneurs and companies apply for government credit and subsidy programs to channel inputs of government-subsidized fuel, seed, and fertilizers to farmers. At harvest time, these intermediaries collect crops from farmers to repay government credit and other production credit provided by commercial and informal sources. Intermediaries are also required to pay income tax and have started charging higher commissions for their services. Due to these taxes, commissions, and fees, the final annual interest rate charged by most intermediaries channeling government credit and providing production credit to farmers has increased to more than 22 percent in 2000.

The lack of an alternative marketing and crediting infrastructure and the reduced presence of reliable traders constitutes one of the most important factors in the breakdown of the rural agricultural economy in the war-affected areas. These unreliable intermediaries have increased the cost of credit while also defaulting on payments to the government and farmers. Commercial banks are reluctant to provide credit to farmers because of the risks of defaults. In addition, fuel and fertilizer companies require payment in advance and have resisted government pressure to provide input material to farmers on credit. Since farmers have been cut off from their traditional sources of production credit and marketing channels, they now rely on these intermediaries to access credit and for marketing products.

During privatization and transformation of socially owned cooperatives, 100 percent of the shares from each cooperative (excluding land) were sold to current and former employees at subsidized prices. This transformation process has been completed in most areas, but this phase of the privatization process resulted in several problems. Croatian Serb employees and others displaced in 1995 did not participate in the transformation process. In addition, the employee ownership structure has created challenges for the Cooperatives to adapt to new market realities. They are characterized by low profitability, excess capacity, and over-employment. Members of these former socialist cooperatives are mainly employees (not farmers). Therefore, farmers have little influence on management and the type of activity undertaken. This conflict of interest persists in the cooperatives and results in poor management/farmer relationships. The participation of Croatian farmers as members in cooperatives is thus very low compared to the United States and the European Union. Cooperatives are also no longer able to effectively finance the purchase of raw materials and supplies, or the purchase and marketing of grains and livestock. As a result, many privatized cooperatives in the war-affected areas are insolvent and have collapsed.

Farmers have quickly learned that their personal economic situation will not improve by marketing their products individually to buyers or by accessing expensive credit. However, farmers in the war-affected areas are currently isolated from the market and from accessing production credit. Donors continue to play an important role in the coordination of efforts to provide marketing assistance and production credit to overcome these problems. There are still opportunities to spur development and encourage return by providing these services and items in certain municipalities where the market is not well developed.

**Best Practices in Croatian Agricultural Association and Cooperative Development**

Since we started the process of forming farmers' organizations in the war-affected areas, tremendous growth has occurred in the number of agricultural associations and cooperatives in Croatia. Numerous NGOs, donors, and the Government of Croatia have also initiated programs to sponsor and support these associations and cooperatives. The focus of this section is to summarize our methodologies used in forming and strengthening farmers' associations and cooperatives in the war-affected areas, and to recommend best practices for donors and organizations providing support to these organizations in the future.

1. ***There must be a strong personal financial interest for farmers joining together.***

The initial focus of our efforts in any municipality or village has been to survey the current capacity of production and needs of the producers to determine a personal reason for farmers to come together. The most common need has been access to markets.

2. ***Modern cooperatives must be formed incrementally.***

Farmers are initially reluctant to join an organization, since many had negative experiences with socialist era cooperatives. Forming an association first, instead of a cooperative has proven the best initial first step for marketing the concept of an independent farmer organization.

3. ***The strongest associations are those having a single purpose from the beginning.***

Associations formed for solely "economic" purposes grow and expand more rapidly. Leaders with this purpose, focus on business activities from the beginning. NGOs should be careful to avoid developing associations with multiple purposes (economic, social, political, etc.) which will result in members dropping out as soon as their primary interest is not given top priority. The primary goal for any such farmer organization is to increase the welfare of its members and to concentrate on the further development of its business activities.

4. ***Initial marketing initiatives should be simple and limited to a single commodity.***

The first joint marketing initiatives have concentrated on selling the product that was most difficult for farmers to sell on their own. This activity is simple, but requires NGOs to assist with locating the buyer, surveying and estimating the volume of products on the individual farms, negotiating price and quality, assembling the product for delivery, arranging for collection of payment, making sure the farmers are paid and retaining a small margin for the association. This successful activity has laid the foundation for larger and more challenging operations in the future, and has laid the groundwork for our USAID-funded grant programs.

5. ***More complex projects can be developed after an initial marketing success.***

Once an initial marketing activity has demonstrated success, more complex programs can be designed with the farmers' support and involvement, such as obtaining credit from buyers and adding consistent delivery dates instead of a single delivery.

6. ***Operations can expand to include non-members and new returnees.***

Non-members of associations were invited to participate in marketing projects, which benefited the entire community by providing an outlet for products. New returnees have immediate access for marketing products through existing associations and did not have to be founders to participate.

7. ***Business activities should focus on market demand and profits.***

Farmers in transition economies experience challenges surviving in a demand driven market economy. Many farmers continue to plant crops and raise livestock that were traditionally produced without considering market demand and expected returns per hectare. NGOs need to assist with market research and cost-benefit analyses for crops to demonstrate new market realities.

8. ***The level of development determines the activities an association can successfully complete.***

NGOs need to recognize the stage of development of the farmer organization they are assisting and help them engage in activities in which they can succeed and which contribute to their development. Farmers almost always recognize needs that are real and pressing that either require resources the association does not have or that the association is not capable of managing. All communities want new tractors, grain storage, delivery vehicles, etc. The NGO community often finances these items before the association has developed to a level where it is capable of managing the new services and resources profitably. Failures can be avoided with careful feasibility studies of the association's abilities, the market of interest, and upstream and downstream activities, inter alia. Failures mean that resources are lost, NGOs are held responsible for the failures, and further development of the association is hampered or even nullified.

9. ***Large and complex projects are difficult to design for a single association.***

The scale of production in many villages and municipalities is not large enough to attract larger processors and more reliable buyers. A single truckload is initially advantageous. However, the fixed cost of organizing single truckloads is higher than a larger scale delivery schedule that will provide a stronger negotiating position with the buyer and other economies of scale. The goal is to obtain the best price from a reliable buyer. Credit or financing also requires groups of associations instead of a single association because of the economies of scale in lending and loan supervision.

10. ***Processing requires a higher level of organization.***

Before introducing value-added processing services, associations need to be transformed into modern agricultural cooperatives. Processing and other value added projects require a significant commitment of funds. For that reason, feasibility studies should be mandatory (including a financial analysis). The level of detail should depend on the level of complexity for each project. The potential of introducing value-added processing also provides an impetus for the formation of cooperatives.

## ATTACHMENT B

### **11. *Transformation of associations into modern cooperatives should be encouraged and supported with technical assistance.***

Transformation of associations into cooperatives should be encouraged and groups unwilling to make this transition should be abandoned or their assistance turned over to other donors. We have often encountered associations that were organized to exist for unclear reasons or just to obtain a donation. Rather than organizing to achieve a common business objective to benefit the group as a whole, which could only be achieved by group action, their interest in staying together appeared to focus on lobbying for donor grants. NGOs should be encouraged to study possible economic activities with these groups that will be feasible and profitable. Once associations are unwilling to focus on group economic activities, NGO efforts with them should cease. NGOs should then consider encouraging the association to seek assistance from another NGO that focuses on funding communities rather than providing economically related technical assistance.

### **12. *Organizational and Business training is essential at the early stage in association and cooperative development.***

Training in organization and management is crucial to insure that the farmer members understand the democratic control principles of the cooperative and the lines of responsibility. Lack of control and accountability of elected Board Members is often weak and leads to dissension and the eventual breakdown of the organization.

### **13. *Modern cooperatives are focused on marketing specific products with high profit margins for their members***

Many association members quickly adopted the concept of shifting production towards select products, which offered the largest margin and were in demand on the Croatian market. Once leaders are capable of managing their proposed activities, an Agricultural Cooperative Model can be introduced to the members. This model is designed for farmers who want to specialize their production activities and to begin providing value-added services and processing. Cooperative models and principles from the United States and Western Europe should be introduced and pursued. These models are based on farmer owned and managed cooperatives that provide patronage refunds to members and operate at cost. This model varies significantly from the current model in Croatia, in which farmers are not sole owners, patronage refunds are not paid to farmers, and cooperatives do not operate at cost. The creation of modern marketing cooperatives in Croatia is embryonic and has been endorsed by the Croatian Government.

### **14. *Flexibility of membership must be encouraged.***

Associations and cooperative members must learn that membership is an active process not static. They will become more successful by taking on new members, where feasible, and eliminating non-productive members. There is a reticence in many organizations towards taking on new members or, where family or community bonds are strong, in eliminating current members. Some members of the community did not initially join the association or others recently returned to the community. Others abandoned the associations once they realized, for example, grants were not immediately forthcoming. Founding members are right to think that new members need to contribute to the association, but should always accept and seriously consider new applications for membership. From the point of view of

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NGOs, working with larger groups is less costly and increasing the size of the association is desirable. Most importantly, ethnic differences exist in many of these communities and it is possible to overcome these differences by combining the groups into a single association or cooperative.

If returnee farmers are initially reluctant to join the organization or do not have the resources to pay membership fees, the farmers' organization should offer production contracts to the non-members. This option allows returnees to immediately market their products through the organization. As they accumulate income from the sale of their products, the returnees can then submit applications and pay membership fees.

**15. *Both production and marketing are key elements to success and should be developed in tandem.***

In Croatia, international NGOs started providing assistance during an emergency situation and their initial task was to feed, clothe, and house returnees. Subsequently, NGOs provided farmers with what they needed to get back into primary agricultural production that existed before the conflict (seeds, hand tools, equipment, etc.). Recently, however, an increasing demand has emerged for marketing assistance as the farmers they are working with find difficulty in marketing products, in part a success of NGOs in production assistance is responsible for creating the surpluses farmers now have difficulty marketing. These NGOs have responded by exploring marketing assistance for these associations.

**16. *Cooperative development requires time.***

We estimate that cooperatives need to be accompanied with a consistent level of technical assistance for up to five years as a reasonable period. Farmers understand the simple concept of coming together to sell a single truckload of products. The leadership of cooperatives will come to understand more complex operations after a number of years of detailed technical assistance in modern management techniques.

**17. *A major component of association building and cooperative development is the development of secondary and higher level associations.***

The key to sustainability for farmer organizations lies in the development of secondary level associations. The development of these higher-level organizations will take time. Higher level organizations are still embryonic or do not exist in Croatia. Their development is crucial for the long-term viability of the organizations. These higher level organizations are the ones that will lobby on relevant issues and will serve as a window to the international community. These higher level organizations can be a force to help obtain other things the community needs and in helping manage stores and grain elevators and in helping the community for community-managed projects such as wells, road maintenance, etc.

**18. *Coordination with outside donors needs to be maintained by the NGO assisting a specific association or cooperative.***

It is necessary to understand the stage of development of an organization and to keep well-meaning donors from drowning the association or cooperative with resources before they are able to manage them. To avoid discord, donor coordination through an umbrella organization should be utilized. This will avoid one donor being played off against another donor; it will

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also insure that associations and cooperatives are able to obtain the resources that they are able to handle and contributes to their growth.

### 19. *Women's participation needs to be enhanced.*

Women's participation should be encouraged to a greater extent than has been observed in the past. Women should be invited to attend meetings, to become members in their own right, and to develop a more direct role in the management of the organizations. At present, they are often represented by their spouses who either do not fully understand what has transpired at a meeting or fail to communicate what was discussed. Also, associations, cooperatives, and NGOs should use part of their resources as loans to women who have non-agricultural microenterprises. This will lower the risk of having all resources exposed to primary agriculture production and will provide working capital to viable enterprises that do not have access to working capital via traditional commercial lenders.

### 20. *As funding for cooperative development projects diminishes, NGOs should focus their funding on the further development of cooperatives already in operation in order to make a larger impact.*

As funds for association and cooperative development become more and more limited, NGOs should concentrate on the sustainability of previously established organizations. A tremendous amount of time, education and financial resources are needed to organize farmers into a cooperative and bring the cooperative to the level where it can operate efficiently and manage production effectively. Therefore, NGOs should continue to support the further development of established cooperatives, where the resources can make a larger impact in a much smaller time frame. Otherwise, by commencing a project with a new group of farmers, NGOs run the risk of not having the time or the resources to develop the organization to a sufficient level of sustainability.

### 21. *US-funded PVOs and NGOs should be encouraged to set up European subsidiaries and encouraged to attract funding from non-US sources.*

US-funded PVOs and NGOs need to attract funding from alternative sources, which could substantially add to their core funding. Many donors are currently limited to a single source of funding to working with European or US funding agencies. Since EU funding is substantial, as well as funding from individual European countries, it's within the interest of US-funded NGOs to set up European operations or subsidiaries in Croatia in order to be eligible for this type of funding.

### 22. *The time for NGO direct intervention and funding for seeds and other basic inputs is ending.*

NGOs should provide more resources and technical assistance in marketing primary agricultural products. The days of gift seeds and fertilizers will be over soon in most areas. Retail stores, including those operated by new cooperatives, link their members with wholesalers and should provide farmers with these items. The situation is different in several municipalities in the former sectors North, South, and West where the market is not well developed, particularly in terms of credit and equipment. There are still opportunities to spur development by providing these items in the areas with recent returnees. These items can

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also be provided through NGO credit programs and payment terms should be at market rates and terms to avoid distorting the market for commercial capital.

**23. *The association or cooperative itself is responsible for the choice of activities in which it wishes to participate.***

Cooperative and association leaders are ultimately responsible for the choice of activities in which to participate and in which to invest their energy and resources. NGOs can guide the organizations but should avoid making decisions for them. If the organization decides to adopt a business service that we do not endorse, we still dedicate resources to helping the organization make that project a success.

**24. *A basic accounting system and tax compliance training is a must for new associations and cooperatives.***

A basic accounting system is a must for new associations and cooperatives and periodic monitoring by NGOs contributes to the development of the accounting system, enabling it to carry out additional and more complex operations in the future. NGOs should emphasize the importance of having transparent bookkeeping and accounting systems. Local trainers can provide seminars for multiple clients for a reasonably low cost to the NGO. Technical assistance and training should be provided to the members on the purpose and benefits of registering as individual taxpayers in order to be included within the Croatian VAT system.

### Avoid Running into Deadends with Grant and Credit Programs

The driving force behind each of our grant projects with farmer organizations has been the ability to market products and to reduce the risk of not being paid by buyers. NGOs need to avoid certain risks such as speculative production and producing without forward contracts. Increasing production on family farms without contracts and reliable marketing options risks losing limited grant and donor funding and, more importantly, risks losing the farmer's investments. A summary is provided for several best practices and recommended methods for lowering the risks of donor grant and credit funds.

**25. *Forward contracts need to be signed with reliable buyers.***

Forward contracting production is a relatively new concept in Croatia. Processors, traders and integrators are initially reluctant to sign forward production contracts. Credit reports can be requested from independent agencies to rate the payment history for many possible buyers. Buyers with the most reliable history should be targeted for signing contracts. Cooperatives are often forced to sign contracts with unreliable partners and should always protect their revenues with bank guarantees or collateral, regardless of the reputation of the buyer.

**26. *Contracts between farmer members and the cooperative reduce risks for the cooperative and screen the less serious farmers from participating in projects.***

Cooperatives should sign contracts with members obtaining credit or producing for a forward contract. This will screen out the less serious farmers and will reduce the risk of the cooperative not meeting obligations contained in the contracts. Cooperatives should require members to provide collateral or guarantees for production credit provided to meet any forward contract.

**27. *Feasibility studies, cash flow forecasts and market research should be completed before committing funds.***

NGOs should thoroughly investigate business plans and proposed activities to eliminate farmer organizations existing solely for the purpose of lobbying for grant funding. If an organization appears to have a clear objective, NGOs should conduct a comprehensive feasibility study and market analysis to confirm the feasibility of the proposed project. If the results of the study and analysis show that the organization's proposed activities are not feasible, NGOs should not solicit a new proposal, but should keep the door open. Projects that are solicited by donors are doomed to failure.

**28. *Technical assistance should be provided to members and to the farmer organization before and during the implementation of grant projects.***

NGOs should focus on providing technical assistance to members and the farmer organization before and during implementation of grant projects. Project success depends on the quality of production delivered from the members and the quality of the marketing organization. Local advisors and consultants are available in Croatia and should be used alongside US and European advisors to develop a cadre of qualified local consultants.

**29. *NGOs should refrain from directly managing the organization and grant project.***

NGOs should always concentrate training resources to support and develop the managers and leaders of the organizations, and should avoid acting as managers for the organization. The leaders will ultimately be held responsible for choosing and implementing its business activities for members.

### **Alternatives for Continued Assistance**

**30. *A national association of independent cooperatives can lobby for reform in taxation, legislation and economic policy in the interest of the farmer members.***

Continued assistance should be provided to support the creation of a national, independent association of agricultural cooperatives. A national association of independent cooperatives is needed to address regulatory and legislative barriers preventing the rapid development of the embryonic agricultural cooperative movement in Croatia.

**31. *An inventory credit program can address the grain marketing problems and limited access to production credit for farmers.***

A national association of cooperatives is an ideal partner for introducing an inventory credit program in Croatia. Since many cooperatives and their members do not have access to commercial lenders, an inventory credit program will enable them to use the grain stored in licensed warehouses as collateral for debt financing from commercial banks.

### **Firm Level Advisory Group (FLAG)**

The Firm Level Advisory Group (FLAG) is an initiative to develop Small and Medium-sized Enterprises (SMEs) and farmer organizations as part of the US strategy to support the return of displaced persons and refugees to the war-affected regions of Croatia. The project is financed by a cooperative agreement from the United States Agency for International Development (USAID) and is implemented by FLAG International LLC under a management agreement with the University of Delaware. Since June 1997, more than 90 US volunteers and consultants have provided technical assistance to SMEs and farmer's organizations in Croatia. FLAG International LLC is responsible for managing and coordinating the delivery of services and managing the program in Croatia.

Training and technical assistance programs are individually designed to assist SMEs and farmer-owned associations/cooperatives to improve internal and financial management, increase output and revenues, strengthen marketing, improve profitability and create sustainable employment and income for populations returning to or remaining in the war-affected areas. We have supported the formation of 33 agricultural associations and cooperatives to service the war-affected areas. These organizations provide benefits to more than 12,500 members.

In 2000, we introduced a grant-component to the ongoing technical assistance program, which is a USAID-sponsored fund to capitalize existing association and cooperative clients. In 2000, twelve grant projects totalling USD 800,000 were designed and implemented to capitalize cooperatives and associations with livestock and equipment. More than 650 farmer members were provided meaningful employment and average annual net income per farmer equalled USD 1,956. The grant projects were leveraged with USD 316,000 in donations, short-term loans and infrastructure reconstruction projects funded by other donors including the Lutheran World Foundation (LWF), Arbeiter-Sammeritar-Bund (ASB), UNDP, Stiftelsen Jaeren Produktutvikling, ICMC, UNOPS, NOA, and IRC. In addition, in CY2000, our expatriate, local staff and consultants completed 16 market surveys and 17 feasibility studies, and organized 52 seminars with 1,116 participants. Twenty-one US Volunteer Advisors and 36 Croatian Consultants completed technical assistance assignments with 54 SME clients and 38 Association and Cooperative clients.

We initially introduced our farmer association model in the former UNTAES region in 1997 and expanded the project and introduced the model to the former UN protected sector North and South in 1999. As the farmer organizations expanded and started to develop more complex projects, the Association Model evolved into a traditional Cooperative Development project. To distinguish the new model from the socialist era cooperatives, we refer to "western style or modern" cooperatives during training, technical assistance, and education programs. In 2000, seven additional cooperatives were organized and registered to specialize in one primary production activity and to begin providing value added services for members.